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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1955

No. 695

CONSOLIDATED EDISON COMPANY OF NEW YORK, INC.,
Petitioner,

v.

THE UNITED STATES,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

Consolidated Edison Company of New York, Inc. prays that a writ of certiorari issue to review the judgment of the United States Court of Claims, entered in the above entitled case on December 6, 1955.

Citation to Opinion Below

The opinion of the Court of Claims, printed in Appendix B, infra, pp. 17-25,[1] is reported in 135 F. Supp. 881, but not yet in the Court of Claims reporter.

Jurisdiction

The jurisdiction of this Court is invoked under 28 U. S. C., Section 1255(1).

[1] All page references, unless otherwise indicated, are to this petition.

Question Presented

Whether under Section 23(c) of the Internal Revenue Code of 1939 a contested real estate tax liability accrues in the year the litigation is ended or, prior thereto, in the year the disputed tax is involuntarily paid.

Statutes Involved

The applicable provisions of the pertinent statutes are set forth in Appendix A, infra, pp. 15-16.

Statement

Petitioner sells electricity and gas in the New York area (finding 1, p. 25) and owns numerous parcels of real estate devoted to its business as a gas and electric utility (finding 5, p. 26). It kept its books and filed its income tax returns on the accrual basis (finding 2, p. 25). The taxable years involved are 1938, 1939 and 1941.

As above stated the question presented in this case involves the determination of the year in which deductions should be taken in respect to the local real estate taxes on these parcels which were contested and unadmitted.

The facts may be conveniently stated by using, instead of actual figures, a hypothetical real estate assessment of $100 for 1939. The parties and the court below adopted this method of concisely stating the issue involved (finding 42, p. 41).

On January 25, 1939 petitioner was notified of a tentative assessment of $100 (in terms of the illustrative example) on its New York City real estate (findings 6, 42, pp. 27, 41). By March 15, 1939 petitioner filed with the New York tax authorities a bona fide protest against this assess-

ment; in this protest petitioner admitted liability of $85 but petitioned for administrative reduction of the assessment by $15 (finding 42, p. 41). The valuation claimed in the protest was based on the best judgment of petitioner's officers and of independent experts (findings 21, 22, 42, pp. 34, 41).

On May 25, 1939, after a hearing, a final assessment of $100 was made (finding 42, p. 41).

Under New York law the institution of a court proceeding to correct an assessment does not postpone the due date of the tax, and failure to pay on the due date subjects the real estate to a lien which can be foreclosed and the property sold (finding 13, p. 30). Accordingly on October 1, 1939, petitioner, under protest and reserving its rights, paid the $100 in order to avoid liens, seizures, levies, penalties, and interest (findings 17, 42, pp. 32, 41).

On October 25, 1939, petitioner instituted proceedings in the appropriate New York State Court to expunge the excessive portion of the assessment; in its petition to review petitioner again admitted liability of $85 but denied liability for the $15 by which the assessment exceeded $85 (findings 18, 20, 42, pp. 33, 41). Petitioner was confident that the valuation it claimed would ultimately be sustained by the court (findings 21, 24, p. 34).

Thereafter, the New York court proceedings were compromised, and on August 21, 1941 an order was entered in those proceedings fixing petitioner's tax for 1939 at $95 (findings 23, 28, 42, pp. 34, 35, 41). In October, 1941 petitioner received back from the New York tax authorities $5 of the originally disputed $15 (finding 42, p. 41).

Decision of Commissioner of Internal Revenue

The Commissioner of Internal Revenue allowed as deductions for "taxes paid or accrued" in 1939 the amounts ultimately determined in 1941 to have been proper ($95)—

and at the same time included in petitioner's gross income for 1941 the refunded overpayments ($5) of the 1939 real estate taxes.

Petitioner's Contention

The petitioner claims that the amount of taxes accrued within a taxable year must be determined in accord with the normal accounting concepts relevant to the accrual basis.

On the basis of the undisputed proofs of record, the Court below found that under recognized accounting principles on the accrual basis, no expense deduction may be had for a liability which is denied (finding 38, p. 39); this principle is equally applicable to disputed local taxes (finding 38, p. 39); the basic concept of accrual accounting is that the flow of cash has no effect upon income or expense determination (finding 36, p. 39); payment of a liability that is denied does not "accrue" it (findings 37, 38, p. 39); and payment of an unadmitted and still contested amount is recorded as an asset in the nature of a deposit or prepayment and not as an income or expense determining transaction (finding 38, p. 39). The Court further found as a fact that under these generally accepted and well recognized principles of accrual accounting the disputed $15 which was paid in 1939 constituted an asset until 1941 when the asset was reduced to $5 (finding 45, p. 42); and that $10 accrued and was deductible as an expense in 1941, and was not to be related back to 1939 (finding 46, p. 42).

Petitioner therefore claims that under Section 23(c), which provides for the deduction of "taxes paid or accrued within the taxable year", the proper amounts deductible in 1939 on the accrual basis were the portions of the assessed taxes admitted by petitioner to have been proper ($85); that of the unadmitted and contested portions ($15) the additional amounts ultimately determined in 1941 to have been proper ($10) were deductible in 1941; and the refund in 1941 of the overpayments ($5) did not constitute income

but an exchange of assets—an exchange of "deposit for contested taxes" for "cash."

Decision of the Court Below

The Court below held* that the *payment* of a disputed tax accrues the tax; therefore the entire amount of the assessed tax ($100), including that which was denied and actively contested in the New York courts ($15), accrued and was deductible under Section 23(c), in 1939; and that the refund of the excess payment ($5) in 1941 upon the termination of the litigation was income to petitioner in that year. In reaching this decision the Court acknowledged that a taxpayer may not accrue taxes for purposes of federal income tax deduction during a year in which he is contesting the taxes and has not paid them over to the tax collector, and that, under generally accepted accounting principles, payment of contested taxes to the tax collector under protest does not make it proper to accrue such taxes. It necessarily followed, therefore, that, if tax consequences were to harmonize with accounting principles, only $85 of the 1939 real estate tax assessment of $100 could be regarded as accrued for purposes of income tax deduction in 1939, even though petitioner actually paid $100 to the New York tax authorities in that year, and that no part of the contested $15 could be deemed accrued as a deduction in 1939. The Court below avoided reaching this conclusion by summarily rejecting the application of generally accepted accounting principles "because such principles represent a refinement in ascertaining net income that would be impractical and, in our opinion, infeasible in the administration of the revenue laws" (Appendix B, p. 24). Having rejected *accepted* accounting principles, the Court followed its own doctrine that payment of contested taxes, even though involuntary, under protest and with the most sincere belief that a refund will be forthcoming, nevertheless accrues them in the full amount of the payment as a deduction in the year in which the payment is made.

* Jurisdiction was based on 28 U. S. C., Section 1491.

Summarizing the foregoing, the Commissioner allowed a $95 deduction for 1939 and taxed $5 in 1941; the court below allowed a $100 deduction in 1939 and taxed $5 in 1941; and the petitioner claims $85 is allowable as a deduction in 1939, $10 is allowable as a deduction in 1941, and the receipt back of the $5 deposit is not income in any year.

Reasons for Granting Writ

1. The decision of the Court below is contrary to the principles of accrual and contrary to the method of determining the amount of such accrual established by this Court in *Dixie Pine Products Co.* v. *Commissioner*, 320 U. S. 516 (1944); *Security Flour Mills Co.* v. *Commissioner*, 321 U. S. 281 (1944); *United States* v. *Olympic Radio and Television, Inc.*, 349 U. S. 232 (1955); and *Lewyt Corporation* v. *Commissioner*, 349 U. S. 237, 242-243 (1955).

(a) The *Dixie Pine* and *Security Flour Mills* cases clearly establish that an accrual basis taxpayer may not accrue and deduct a tax liability which is denied and contested until the year in which the litigation is ended.

Dixie Pine held that the denial and contest of the State tax liability made that liability "contingent," rather than "fixed and certain," even though the State statute imposed upon the taxpayer a definite, fixed and certain obligation to pay the disputed tax; and that, therefore, the disputed tax liability did not accrue and become deductible, under Section 23(c), in a year prior to the year in which the litigation terminated (320 U. S. 516, 519).

The Court below, however, held that the contested real estate tax liability did accrue and become deductible before the litigation ended because of its payment, "even though payment is made under protest and even though litigation

is started within the taxable year to obtain repayment." (p. 24). But an involuntary payment[2] of a contested tax liability makes that liability no less contingent nor more fixed and certain, for purposes of accrual and deduction under Section 23(c), than does the statutory obligation to pay the tax—the outcome of the litigation must still be awaited to fix and determine the extent and amount of the contested tax liability.

It is not merely the payment of an item, but rather the nature or character of the item paid, that determines its accruability or deductibility.[3] Admittedly, the contested tax liability was not accruable or deductible a moment before it was paid. There is nothing in any concept of accrual which transforms a non-deductible item into a deductible one by an involuntary payment. Payment under such circumstances simply creates another capital asset—a deposit for contested taxes—to take the place of the cash turned over to the local tax authorities (finding 38, p. 39).[4]

The situation in the instant case is, for all practical purposes and in economic reality, not unlike that in *Security Flour Mills* where the taxpayer, under Court order, paid the disputed tax to a bank designated by the Court. The flour mill was as much out-of-pocket the amount of the disputed taxes paid to the bank under the Court order as was petitioner when it involuntarily paid the disputed tax to the City of New York. In both instances the payment was made subject to repayment depending upon the outcome of the litigation; and in both instances the liability for the disputed tax remained contingent and uncertain until the litigation was terminated.

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[2] See *People ex rel. Wessel, Michel & Gross* v. *Craig*, 236 N. Y. 100, 104; 140 N. E. 209 (1923) as to the involuntary nature of the payment of contested New York real estate taxes.

[3] Cf. *Commissioner* v. *Boylston Market Ass'n.*, 131 F. 2d 966 (1st Cir., 1942) (prepaid insurance); *Cooperstown Corporation* v. *Commissioner*, 144 F. 2d 693, 696 (3rd Cir., 1944), *cert. denied*, 323 U. S. 772 (payment of nonexistent tax liability).

[4] See *Commissioner* v. *Boylston Market Ass'n.*, *supra*, at p. 968.

By predicating its decision upon payment, the Court below introduced a wholly alien concept to the principles of accrual established in *Dixie Pine* and *Security Flour Mills,* and thereby substituted and prescribed "a divided and inconsistent method of accounting not properly to be denominated either a cash or an accrual system" (*Security Flour Mills,* 321 U. S. at p. 287).

(b) *Olympic Radio* held that the phrase "paid or accrued" as used in the various sections of the income tax law must be uniformly construed to mean "paid" by a cash basis taxpayer or "accrued" by an accrual basis taxpayer.

The Court below has in effect nullified this ruling by giving the term "accrued", as used in Section 23(c), a meaning which is contrary to the acknowledged principles of accrual. It engrafts upon the concept of accrual the criterion of payment—a criterion that is solely applicable to the cash method of accounting—and thereby accomplishes, indirectly, that which this Court held it may not do, directly.

(c) The *Lewyt* case followed the ruling in *Olympic Radio* and, in addition, stated that "the amount of tax accrued within the taxable year * * * is to be determined in accord with the normal accounting concepts relevant to the accrual basis" and that "when an amount is arrived at by proper application of recognized accounting principles on the accrual basis, the test of [the statute] has been met." (349 U. S. at pp. 242-243).

The Court below, however, refused to follow this principle, and held that the amount of local real estate taxes to be accrued and deducted under Section 23(c) is to be determined by the amount of cash paid even though such treatment was directly contrary to the recognized accounting principles on the accrual basis which the Court itself found to be applicable.

2. The extent to which accounting concepts determine the propriety of tax accruals for income tax purposes is a question of importance in the administration of the income tax laws.

The decision of the Court below strikes at basic principles of statutory construction important to the understanding and administration of the income tax laws. Section 41 of the 1939 Code (p. 15) provides for the computation of a taxpayer's net income "in accordance with the method of accounting regularly employed in keeping the books of such taxpayer"; Section 43 (p. 16) provides that deductions shall be taken in the year paid or accrued "dependent upon the method of accounting upon the basis of which the net income is computed"; and Section 48 (p. 16) provides that "the terms 'paid or incurred' and 'paid or accrued' shall be construed according to the method of accounting upon the basis of which the net income is computed". These provisions, as well as that of Section 23(c), have been substantially reenacted in the Internal Revenue Code of 1954.

In addition to creating doubt in areas believed to have been definitively determined by this Court, the decision below seeks to create an unnecessary and unwarranted difference between income tax accrual and generally accepted principles of accrual accounting, thus reversing the long trend toward coordination between income tax and accounting principles.

From the very beginning this Court has sought to harmonize the two principles. In *United States* v. *Anderson*, 269 U. S. 422, 440 (1926), it was stated that Congress intended in the Revenue Acts "to enable taxpayers to keep their books and make their returns according to scientific accounting principles". And, as already noted (p. 8), only recently it was stated in *Lewyt* that "where an amount is arrived at by proper application of recognized accounting principles on the accrual basis the test of [the statute] has been met".

It is of paramount public interest that unnecessary differences between income tax and accounting principles be avoided wherever possible. Harmony between the two should be the rule and conflict between the two the exception. An artificial exception of judicial origin in respect of one type of deduction casts doubt and uncertainty upon all types of deduction.

The decision of the Court below creates such an artificial exception and, in addition to being contrary to the principles established by this Court, brings uncertainty to the construction of the income tax statute as to the accrual of all types of deductions. If payment could remove the non-accruable and non-deductible character of a contested tax liability it would follow that payment could remove those characteristics from other items which have been held to be non-deductible.[5] Taxpayers on the accrual basis —and "most corporations are on the accrual not the cash basis" (*Olympic Radio*, 349 U. S. at p. 236)—may not feel safe, under the decision of the Court below, in using scientific accounting principles to determine their income tax liabilities.

It is believed the decision of the Court below is contrary to the decisions of this Court above cited (pp. 6, 9) and of the Courts of Appeals for the First Circuit and the Third Circuit above cited (p. 7). If it is not, then the Court of Claims decided an important question of federal income tax law which has not been, but should be, settled by this Court.

3. The decision of the Court below is erroneous on its own facts and reasoning.

The Court below found (finding 44, p. 42) that, under accepted and well recognized principles of accounting, the proper entries with respect to the $100 were: in 1939, to charge $85 as tax expense and to set up an asset account

[5] See cases in note 3, p. 7.

of $15 as deposit for contested taxes; and in 1941, to charge $10 as tax expense and to record the receipt of $5 as a return of the remaining unapplied deposit for contested taxes. The Court disregarded these findings

> "because such [accounting] principles represent a refinement in ascertaining net income that would be impractical and, in our opinion, infeasible in the administration of the revenue laws". (p. 24).

There is no evidence of record or finding in this case of impracticality or infeasibility; nor does the Court below explain in what respects it would be impractical or infeasible.

On the contrary, it would appear to be impractical and infeasible *not* to follow the objective criteria of recognized accounting principles in administering the revenue laws. (1) It would encourage administrative officers to disregard established principles whenever it would be in the interest of the revenue to do so, and to justify such arbitrary action on the ground of impracticality or infeasibility in the administration of the revenue laws; (2) it would also create an arbitrary difference in income tax consequences between taxpayers residing in states which permit contest of local taxes before payment and taxpayers residing in states which require payment before contest; and (3) the novel rule established by the Court below would change the fixed standard of accrual under accounting principles to a shifting standard of accrual dependent upon the time the taxpayer chooses, for his own convenience and tax benefit, to pay the contested tax.

The decision below purports to follow that Court's earlier decision in *Chestnut Securities Co.* v. *United States,* 104 C. Cls. 489, 62 F. Supp. 574 (1945). That decision was predicated upon the theory that "it is hardly conceivable that a liability asserted against him [taxpayer], which he has discharged by payment, has not 'accrued' within the meaning of the tax laws and the terminology of accounting. Accrual, from the debtor's standpoint, precedes payment,

and does not survive it". (104 C. Cls. at pp. 494-495; 62 F. Supp. at p. 576). But the findings of the Court below as to the applicable accounting principles (findings 35 to 38 inclusive, pp. 38-39) directly contradict this theory. In fact, the Court itself recognized this and abandoned that theory when it stated "What we have said does not mean that the mere payment of an item accrues that item, * * *" (p. 24).

In justification of its conclusion, however, the Court went on to state "but rather we hold that payment of an item which is *otherwise accruable* in the taxable year accrues that item, even though payment is made under protest and even though litigation is started within the taxable year to obtain repayment". (emphasis supplied). Whether the phrase "otherwise accruable" means "otherwise accruable but for the payment", or "otherwise accruable but for the denial and contest of liability", it is apparent that the Court below either prejudged the question in issue and predicated its decision on a theory directly contrary to *Dixie Pine,* or attempted to carve out an unwarranted exception to *Dixie Pine.* See supra, pp. 6-10. In either event the decision of the Court below was not based on the aforementioned principle of *Chestnut Securities* that payment, without more, accrues a contested liability and that this is in accord with applicable principles of accrual accounting.

Another ground upon which the Court below sought to justify its conclusion was that the determination of the year in which expenses are incurred and accrue for tax purposes under the accrual method of accounting is to be made "from a practical, not a technical legal test. *Lucas* v. *American Code Co.,* 280 U. S. 445, 449" (p. 23). But in the *American Code* case this Court resorted to the practical test only because "no definite legal test is provided by the statute for the determination of the year in which the loss is to be deducted". (280 U. S. 445, 449). It is submitted that the decisions of this Court in *Anderson, Dixie Pine, Security Flour Mills* and *Lewyt,* all of which deal with

the construction of the statutory "accrual" of taxes, have established a definite legal test of accrual which is controlling herein. Furthermore, the practical test applied in the *American Code* case, resulted in this Court ruling that where liability is contested, the loss is not sustained until the contest is actually terminated.

It is submitted that the very reasoning and findings of the Court below demonstrate its conclusion to be erroneous.

Conclusion

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX A

Internal Revenue Code of 1939:*

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * *

(c) *Taxes generally.*—Taxes paid or accrued within the taxable year, * * * [with exceptions not material here].

* * *

(26 U. S. C. 1946 ed., Sec. 23)

SEC. 41. GENERAL RULE.

The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income. * * *

* * *

(26 U. S. C. 1946 ed., Sec. 41)

SEC. 42. PERIOD IN WHICH ITEMS OF GROSS INCOME INCLUDED.

The amount of all items of gross income shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under section 41, any such amounts are to be properly accounted for as of a different period. * * *

* * *

(26 U. S. C. 1946 ed., Sec. 42)

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* The provisions of the Revenue Act of 1938 which were applicable to the calendar year 1938 and to Oct. 29, 1939 when the Internal Revenue Code became effective, were the same.

SEC. 43. PERIOD FOR WHICH DEDUCTIONS AND CREDITS TAKEN.

The deductions and credits (other than the dividends paid credit provided in section 27) provided for in this title shall be taken for the taxable year in which "paid or accrued" or "paid or incurred", dependent upon the method of accounting upon the basis of which the net income is computed, unless in order to clearly reflect the income the deductions or credits should be taken as of a different period. * * *

* * *

(26 U. S. C. 1946 ed., Sec. 43)

SEC. 48. DEFINITIONS.

When used in this title——

* * *

(c) *Paid, Incurred, Accrued.*—The terms "paid or incurred" and "paid or accrued" shall be construed according to the method of accounting upon the basis of which the net income is computed under this Part.

* * *

(26 U. S. C. 1946 ed., Sec. 48)

APPENDIX B

IN THE

UNITED STATES COURT OF CLAIMS

Nos. 49654, 49655 and 50432

(Decided December 6, 1955)

CONSOLIDATED EDISON COMPANY OF NEW YORK, INC. v. THE UNITED STATES

Mr. James K. Polk, for the plaintiff. *Messrs. Robert E. Coulson, Harold F. Noneman,* and *Gerald D. Groden* were on the briefs.

Mr. John A. Rees, with whom was *Mr. Assistant Attorney General H. Brian Holland,* for the defendant. *Messrs. Andrew D. Sharpe* and *Lee A. Jackson* were on the briefs.

LITTLETON, *Judge,* delivered the opinion of the court:

The plaintiff sues to recover income taxes alleged to have been overpaid for the calendar years 1938, 1939 and 1941. The plaintiff kept its books and filed its income tax returns upon the accrual basis. The primary issue presented in these three cases is what year is the proper year for deduction of contested real estate taxes where payment of the full amount of the tax assessed was made to the City and State of New York within the taxable years, but the correct amount of the liability was not settled until a subsequent taxable year.

The facts, which are fully set forth in the findings, are summarized for the purposes of this decision as follows:

The plaintiff is a public utility corporation engaged in the manufacture, distribution and sale of electrical energy

and gas. During the years involved the plaintiff owned many hundreds of parcels of real estate in the City of New York which were subject to a tax under the laws of the State and City of New York on real estate owned by corporations.

Each parcel of real estate was appraised by the City Tax Commission and its value was placed upon a tentative assessment roll. Administrative proceedings were available to plaintiff to correct erroneous valuations. An application for correction of assessment (sometimes called a protest) had to be filed on forms supplied by the Tax Commission and all pertinent questions thereon had to be answered. One of the questions in the protest which had to be answered was "What do you consider was the full value of the property on January 25 of this year?" Failure to answer this question was fatal to the application. Judicial review was available by way of a certiorari proceeding, an exclusive remedy, only upon exhaustion of the administrative procedure.

In all cases, except where illegality of the tax in its entirety was alleged rather than to its form or method, the petition for judicial review had to set forth, as did the plaintiff's original protest, what the full value of the property was claimed to be. Thus in complying with the requirement of the law of New York, and alleging both in the protest and in the petition to the court the claimed full value of the property involved, a taxpayer admitted liability for real estate tax thereon in a certain and definite amount, namely, the claimed value of the property multiplied by the established tax rate.

The institution or pendency of litigation for the correction of an assessment did not postpone the dates the bills for the real estate taxes became due and payable. Failure to pay the tax bills when due subjected the property involved to a tax lien which had the effect of a judgment lien which could have been foreclosed and the property sold. In addition, a penalty of interest at 7 percent per annum

was incurred. There was no provision in the New York law for suspending or removing the tax lien, whether by injunction, bond or otherwise, other than by payment of the taxes thereon, as billed. Thus an aggrieved property owner had to first pay the real estate taxes and then seek to rectify the error by the exclusive remedy or run the risk, in addition to incurring 7 percent interest, of having the tax lien foreclosed and the property sold.

The parties have agreed that the facts are accurately reflected in the following simplified example, for the taxable year 1939, which is applicable to all the years involved. For the year 1939 plaintiff was notified, on January 25, 1939, of a tentative assessment for real estate taxes in the amount of $100. Within the statutory period and by March 15, 1939, plaintiff, based upon the best judgment of its officers, duly filed a bona fide protest admitting liability in the amount of $85, and petitioning for an administrative reduction of the tentative assessment in the amount of $100 by the amount of $15. After a hearing duly held, and on or about May 25, 1939, final assessment was made in the amount of $100. Thereafter, on or about October 1, 1939, under protest and for the stated purpose of avoiding liens, seizures, levies, penalties, interest, etc., and reserving all rights, plaintiff made payment of the assessed tax in the amount of $100. Within the statutory period, on October 25, 1939, certiorari proceedings were instituted admitting liability in the amount of, and denying liability in excess of, $85. On August 21, 1941, the Supreme Court of the State of New York entered its order in the certiorari proceedings fixing the tax liability at $95. In October 1941, plaintiff received a refund of the excess payment in the amount of $5.

The plaintiff accrued on its books and deducted on its Federal tax returns for 1939 the full $100. Upon audit the Commissioner of Internal Revenue allowed only $95 for that year, but included the $5 refund received in 1941, as

income for 1941. The defendant now concedes that if only a $95 deduction is allowed for 1939, then the $5 refund should not be included as income in 1941. Timely claims for refunds based upon, among other things, an understatement of depreciation and amortization for 1938, 1939, and 1941 were made and partially allowed by the Commissioner. However, the Commissioner offset these refunds by adjustments made because of his treatment of the real estate tax involved in this case.

The defendant raises pro forma the question of the statute of limitations in cases Nos. 49654 and 49655. It states that since plaintiff filed its claims for refund for 1938 and 1939, on March 10, 1942, and March 11, 1943, respectively, plaintiff could have sued within six months thereafter and therefore its petitions in those two cases, filed on May 25, 1950, are barred by 28 U. S. C. § 2501. This question has been decided by our decision in *Detroit Trust Company* v. *United States*, 131 C. Cls. 223, where we held that § 3772 of the Internal Revenue Code of 1939, as amended, was the governing statute of limitations and that the six-year statute of limitations contained in 28 U. S. C. § 2501 was not applicable. The petitions in all three of plaintiff's cases were therefore timely filed.

The plaintiff contends that it should be allowed deductions in 1938, 1939, and 1941 of the amounts of real estate taxes admitted in those years to have been due ($85); deductions in 1941 upon termination of the litigation of the additional amounts of taxes determined to be due over and above the amounts previously admitted ($10); and exclusion from 1941 income of amounts of excess payments of real estate taxes in the prior years which were refunded in 1941 ($5). The defendant's present position is that plaintiff is entitled to deductions in 1938, 1939, and 1941 of amounts of real estate taxes paid in those years ($100), and the inclusion in 1941 income of the amounts of excess payments of real estate taxes for those years which were refunded in 1941 ($5).

The pertinent provisions of the applicable sections of the Internal Revenue Code (26 U. S. C.) are set forth below.[1]

The plaintiff's argument is twofold. First, it argues that in order to accrue a deductible item, admission or absence of denial of liability is necessary, relying on *United States* v. *Anderson*, 269 U. S. 422; *Dixie Pine Products Co.* v. *Commissioner*, 320 U. S. 516, and *Security Flour Mills Co.* v. *Commissioner*, 321 U. S. 281. Second, it argues that generally accepted accounting principles require that the disputed portion of a tax liability, although paid, should not be accrued until liability is established. The plaintiff, citing *United States* v. *Olympic Radio & Television, Inc.*, 349 U. S. 232, and *Lewyt Corporation* v. *Commissioner*, 349 U. S. 237, contends that these recognized accounting principles are highly persuasive on questions of accruals.

The defendant contends that our decision in *Chestnut Securities Co.* v. *United States*, 104 C. Cls. 489, is controlling.

In our opinion the rule stated in the *Chestnut Securities* case is applicable in the instant case. In that case the taxpayer, on the accrual basis, paid 1936, 1937 and 1938 state taxes after a District Court decision in 1940. The Circuit Court affirmed and the Supreme Court denied certiorari in 1942. The taxpayer contended in a suit in this court that the state taxes were deductible in 1940 when paid and the

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[1] Sec. 23. Deductions from gross income. In computing net income there shall be allowed as deductions: * * * (c) Taxes generally. * * * Taxes paid or accrued within the taxable year * * *.

Sec. 41. General rule. The net income shall be computed upon the basis of the taxpayer's annual accounting period * * * in accordance with the method of accounting regularly employed in keeping the books of such taxpayer * * *.

Sec. 43. Period for which deductions and credits taken. The deductions and credits * * * provided for in this chapter shall be taken for the taxable year in which "paid or accrued" or "paid or incurred", dependent upon the method of accounting upon the basis of which the net income is computed, unless in order to clearly reflect the income the deductions or credits should be taken as of a different period. * * *

Sec. 48. Definitions. When used in this chapter—(c) "paid or incurred," "paid or accrued." The terms "paid or incurred" and "paid or accrued" shall be construed according to the method of accounting upon the basis of which the net income is computed under this Part.

defendant contended that they were deductible in 1942 when the litigation was finally decided. We held they were deductible in 1940 because payment discharged the liability and accrued the taxes in that year. The Commissioner of Internal Revenue has adopted and is following this rule. C. B. 1947–2, G. C. M. 25298, pp. 39, 43, 44. The plaintiff asserts that the case is either distinguishable or erroneous.

It is settled that a taxpayer may not accrue an expense when he is denying liability and refusing and contesting its payment. *Dixie Pine Products Co.* v. *Commissioner, supra; Security Flour Mills Co.* v. *Commissioner, supra.* The plaintiff argues from this principle that there must therefore be an admission or absence of denial of liability before an item may be accrued and that the payment of the liability within the taxable year has no effect on its accrual since payment was made under protest and litigation was immediately started to obtain a repayment. This is not necessarily true.

Under the accrual system of accounting revenues are accrued as nearly as practicable to the period earned and expenses, which include taxes, are accrued in the period and against the revenues they helped to produce. Our system of taxation requires a determination of taxes on an annual basis predicated on the economic events which occurred and were in existence during a taxable year. *United States* v. *Anderson, supra; Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359; *Security Flour Mills Co.* v. *Commissioner, supra.* The Supreme Court stated that:

> • • • Only by such a system is it practicable to produce a regular flow of income and apply methods of accounting, assessment, and collection capable of practical operation. • • • [*Burnet* v. *Sanford & Brooks Co., supra,* at p. 365; *Security Flour Mills Co.* v. *Commissioner, supra,* at p. 286.]
>
> • • • The uniform result has been denial both to Government and to taxpayer of the privilege of allocating income or outgo to a year other than the year of actual receipt or payment, or, applying the accrual basis, the year in which the right to receive, or the

> obligation to pay, has become final and definite in amount. * * * [*Security Flour Mills Co.* v. *Commissioner, supra,* at pp. 286, 287.]

When expenses are incurred and therefore should be accrued under the accrual method of accounting for tax purposes, is determined from a practical, not a technical legal test. *Lucas* v. *American Code Co.*, 280 U. S. 445, 449.

Insofar as the plaintiff in the instant case was concerned it incurred an obligation in the amount of $100 in 1939, since it, as a practical matter, had to and did discharge the full amount of the real estate taxes assessed. Its obligation to pay, insofar as the taxable year 1939 was concerned, had become final and definite in amount when it paid the full amount of the real estate tax for 1939 assessed in that year. Viewing the situation at the end of that taxable year, as we must, we find that the plaintiff incurred and paid a $100 obligation, although it was under protest and with the bona fide expectation that a part of the payment would be subsequently refunded.

The plaintiff actually accrued on its books and deducted in its tax returns the full $100 amount. We think this was proper because the plaintiff incurred an expense in the amount of $100 in that year. Had the plaintiff failed to obtain a repayment of its real estate taxes for 1939, its returns would have correctly reflected its income for that year under the accrual method. There is no compelling reason why a sustained expense should be postponed until settlement of the question of repayment. Since the plaintiff was successful and obtained a repayment of $5, under our annual accounting concept this amount should be included as income in 1941, the year plaintiff's right to the repayment became final.

The underlying reason for the rule in the *Dixie Pine Products* and the *Security Flour Mill* cases of refusing a deduction where the taxpayer has not paid the expense and is contesting it, is because the expense may never be in-

curred. In the instant case the expense had been incurred and actually paid within the taxable year and is therefore deductible in that year.

What we have said does not mean that the mere payment of an item accrues that item, but rather we hold that payment of an item which is otherwise accruable in the taxable year accrues the item even though payment is made under protest and even though litigation is started within the taxable year to obtain repayment. Therefore, the plaintiff's prepayment in 1941 of part of its 1942 taxes does not accrue those taxes in 1941.

The plaintiff's argument based upon the fact that accepted accounting principles require that the disputed portion of the tax liability, although paid, should not be accrued until settlement of the dispute, lacks sufficient persuasiveness, under the facts presented in this case, because such principles represent a refinement in ascertaining net income that would be impractical and, in our opinion, infeasible in the administration of the revenue laws.

In view of the complex computations involved in these three cases, the parties have agreed upon computations of the amounts of income taxes overpaid or underpaid by the plaintiff dependent upon which of the alternatives the court finds to be correct. These computations are set forth in finding 47. We hold that finding 47 (C) sets forth the correct deductions and inclusions. Finding 47 (C) provides for the "allowance as deductions in 1938, 1939 and 1941 of amounts of real estate taxes paid in those years ($100.00); and inclusion in 1941 income of the amounts of excess payments of real estate taxes for said years that were refunded in 1941 ($5.00)." Translated into dollar amounts in the individual cases, according to this finding, the plaintiff is entitled to recover $128,329.55 in case No. 49654; $105,305.58 in case No. 49655, and nothing in case No. 50432.

Judgment will be entered for plaintiff in case No. 49654 in the amount of $128,329.55, and in case No. 49655 in the

amount of $105,305.58, with interest thereon, respectively, as provided by law. The petition in case No. 50432 is dismissed.

LARAMORE, *Judge;* MADDEN, *Judge;* WHITAKER, *Judge;* and JONES, *Chief Judge,* concur.

FINDINGS OF FACT

The court, having considered the evidence, the briefs and argument of counsel, and the report of Commissioner Richard H. Akers, makes the following findings of fact:

1. The plaintiff is a public utility corporation duly organized and existing under and by virtue of the laws of the State of New York, with its principal office located at 4 Irving Place, Borough of Manhattan, City and County of New York, in the State of New York, and is engaged in the manufacture, distribution and sale of electrical energy and gas.

2. The plaintiff sues to recover income taxes alleged to have been overpaid for the calendar years 1938, 1939 and 1941. At all times during those years, the plaintiff kept its books and filed its income tax returns upon an accrual accounting basis.

3. Certain formal facts with respect to the years involved herein are as follows:

	1938	1939	1941
(a) Final return filed pursuant to extension duly granted, on or before	6-15-39	6-15-40	6-15-42
(b) Tax liability disclosed	$1,920,881.31	$3,003,304.48	$7,449,126.26
(c) Tax paid in almost equal quarterly annual installments	$1,920,881.31	$3,003,304.48	$7,449,126.26
(d) Refund claims filed within statutory period	3-10-42	3-11-43	(1) 3-12-45 (1) 5-20-46 (2) 6-30-50 (3) 5- 4-51
(e) Amount of Refund Claims	$1,920,881.31	$3,003,304.48	(1) $7,449,126.26 (2) 3,095,705.31 (3) 3,269,864.00
(f) Amount of Refund (Deficiency) determined by Commissioner	$218,897.25	$164,387.86	($402,163.19)
(g) Refund (Deficiency) plus statutory interest received (Paid)	9-9-48	9-9-48	(3-17-50)
(h) Claim rejected to extent not theretofore allowed	9-16-48	9-16-48	(1) 8-8-50

4. The refund claims filed for the years 1938, 1939 and 1941 were based upon the alleged understatement of several deductions, among which were the deductions for depreciation and amortization. In a consideration of those claims, increased deductions for depreciation and amortization were allowed by the Commissioner of Internal Revenue for the years 1938, 1939 and 1941, but they were offset by other adjustments made by the Commissioner, chief of which were (1) the disallowance of that part of the real estate tax deductions taken in 1938 and 1939, which were refunded to the plaintiff in 1941, and (2) the inclusion of those refunded real estate taxes (including a refund of part of the real estate taxes paid in 1940) in the plaintiff's gross income for 1941. In addition thereto, the Commissioner disallowed the plaintiff's claim for an increase of $8,108,497.64 in its deduction for real estate taxes for 1941.

The allowances and the offsetting adjustments made by the Commissioner are shown in the following tabulation:

	1938	1939	1941
(a) Taxable income reported in return	$20, 486, 078. 62	$22, 825, 720. 99	$30, 170, 497. 85
(b) Deduction taken in return for depreciation and amortization	14, 312, 227. 34	14, 805, 412. 97	15, 723, 734. 75
(c) Deduction taken in return for New York City real estate of corporations taxes	12, 697, 226. 61	12, 025, 877. 80	11, 479, 381. 95
(d) Taxable income, as reduced (increased) by Commissioner	26, 904, 030. 95	27, 269, 022. 19	(49, 497, 709. 45)
(e) Decrease (increase) in taxable income as found by Commissioner (a) minus (d)	1, 582, 048. 67	1, 556, 697. 20	(1, 297, 300. 61)
(f) Increased depreciation and amortization allowed by Commissioner	2, 508, 330. 72	2, 155, 149. 66	670, 294. 72
(g) Offsetting adjustments made by Commissioner			
—Reduced real estate tax deduction by	716, 311. 60	622, 260. 26	
—Included in gross income receipt of refund of real estate taxes paid in 1938, 1939 and 1940 aggregating			1, 845, 679. 75

5. During the years involved herein, the plaintiff owned many hundreds of parcels of real estate in the City of New York which were subject to a real estate of corporations tax (hereinafter referred to as real estate tax) under the laws of the State of New York and of the City of New York in

general, and the New York State Tax Law, the New York City Charter and the Administrative Code of the City of New York in particular.

6. The New York City Charter, which became effective January 1, 1938, changed the operating year of the City of New York from a calendar year basis to a fiscal year basis of July 1 to the following June 30, commencing with July 1, 1939. Thereunder, each parcel of real estate, identified by section, block, lot and identification number, is appraised by the City Tax Commission as of January 25; the value so determined is placed upon a tentative assessment roll which is open for inspection from February 1 to March 15; an aggrieved property owner could then seek an administrative review to correct any claimed erroneous valuation by filing with the Tax Commission, on or before March 15, a sworn application for correction of the assessment setting forth the bases and grounds thereof, and could request an oral hearing thereon; a final determination must be made on or before May 25; and if no action is taken by then, the tentative assessment becomes final.

The assessment roll is then sent to the Comptroller of the City of New York who, between June 20 and June 25, prepares a proposed budget for the ensuing fiscal year and submits it, together with the assessment roll and his estimate of revenues to be raised from real estate taxes and from other sources, to the City Council. On the basis thereof, the Council must by June 25 adopt a budget and fix a real estate tax rate which, after considering revenues from other sources and when applied to the final valuation of the assessment roll, will produce the necessary revenue to meet the operating and budgetary requirements of the City for the ensuing year.

Bills for the real estate tax on each parcel—the product of the tax rate thus established and the valuations on the final assessment roll—are then sent to each property owner and are payable in two installments, October 1 and April 1 of the fiscal year.

7. An application for correction of assessment (sometimes called a protest), referred to in finding 6, must be filed on forms supplied by the Tax Commission and all pertinent questions thereon must be answered. Objections which can be raised are (1) overvaluation, (2) inequality, or (3) illegality. Overvaluation or inequality does not invalidate the tax or the liability therefor but merely calls for correction of the amount of the tax. Where illegality is predicated upon an illegal form or method of valuation, it is another way of raising the question of overvaluation or inequality; only where it is addressed to the validity of the tax itself does a successful challenge wipe out the tax in its entirety and all liability therefor.

8. One of the questions in the protest which must be answered is "What do you consider was the full value of the property on January 25 this year?" A similar question was in the protest forms for earlier calendar years. Failure to answer this question is, under New York law, fatal to such application. The Tax Commission causes each protest to be examined to ascertain whether this question is answered, and if it is not, the protest is summarily rejected. Without answering this question, it is impossible to obtain an administrative review of any real estate assessment in New York City.

9. Similar administrative procedures existed prior to the adoption of the New York City Charter, which became effective January 1, 1938, except that the dates set for the various administrative steps to be taken in the earlier years were moved back to fit in with the calendar year, so as to afford similar time intervals for the commencement and termination of the administrative steps. The City Charter retained the year 1938 on a calendar year basis and specific provisions were made for the transition period January 1, 1939 to June 30; for example, the valuations determined for the year 1938 constituted the valuations for this interim period subject to modification for additions and retirements, and the protests filed with re-

spect to the 1938 valuations were considered applicable to the same valuations for the interim period.

10. Under the New York law, an aggrieved property owner could not obtain a judicial review of a protested assessment without first exhausting the administrative procedure outlined. Upon failure to obtain satisfactory relief through administrative process, judicial review could then be instituted not later than October 25 (July 1 for 1938 and the first half of 1939) of the year in which the assessment becomes final.

Article 13 of the New York State Tax Law specifically provides for such judicial review (hereinafter referred to as certiorari proceeding). This is an exclusive remedy. Pursuant thereto, a verified petition to review the assessment must be submitted to an appropriate court or judge; an order thereon is issued directing the issuance of a writ of certiorari to the Tax Commission returnable on a specified date; and the issues raised upon the return date are thereafter brought to trial. In the case of properties as large as those owned by the plaintiff herein, it is virtually impossible to get a judicial determination of the issues raised within one and a half to two years after the cases are started.

11. The petition must explicitly and fully set forth the basis upon which the relief is sought: if it is overvaluation, the extent of the overvaluation must be alleged; if it is inequality, the instances of such inequality and the extent thereof must be alleged; and if it is illegality, the grounds of illegality must be specified. In all cases, except where illegality is addressed to the tax in its entirety rather than to its form or method, the petition must set forth, as did the original protest, what the full value of the property is claimed to be.

Under New York law, the petitioner is bound by the valuation thus alleged as the minimum value that could be found by the court. Thus, in complying with the require-

ment of the law of New York, and alleging both in the protest and in the petition to the court the claimed full value of the property involved, a taxpayer admits liability for real estate tax thereon in a certain and definite amount, namely, the claimed value of the property multiplied by the established tax rate.

12. The real estate tax rate for any particular operating year does not vary or change after it is established. The budget makes provision for estimated refunds of real estate taxes resulting from reductions in assessed valuations, and if the actual refunds exceed that estimate, the tax rate for the year involved is in no way affected thereby. To meet such additional expenditure, the City would have to borrow money therefor and then provide for payment of the loan in the budget of the following year or years, but the City Council does not reopen the budget of the year involved or change the tax rate already established for that year.

13. The institution or pendency of litigation for the correction of an assessment does not postpone the dates the bills for the real estate taxes become due and payable. Notwithstanding the pendency of such litigation, failure to pay the bills when due subjects the property involved to a tax lien which has the effect of a judgment lien and which could be foreclosed and the property sold. In addition, 7 percent per annum penalty interest is incurred.

There is no provision in the New York law for suspending or removing the tax lien, whether by injunction, bond or otherwise, other than by payment of the taxes thereon, as billed. Under the New York law an aggrieved property owner must first pay the real estate taxes thereon and then seek to rectify the error by the exclusive remedy outlined in the statute, or else run the risk, in addition to incurring a 7 percent interest penalty, of having the tax lien foreclosed and the property sold.

14. Immediately prior to the years involved herein, the Board of Taxes and Assessments (as the Tax Commission

was then known) had departed from the usual procedure of valuing each and every parcel of real estate and making individual assessments thereon by section, block, lot and identification number, and consolidated the assessments on the properties owned by the plaintiff into lump sum company assessments for the calendar years 1936 and 1937. These assessments were substantially in excess of the sum of the valuations theretofore assigned to the individual properties. The assessments were contested on the grounds of overvaluation and inequality and also illegality because of the lump sum company assessments.

15. For 1938 and subsequent years, the lump assessment procedure was discontinued and tentative assessments were made upon the individual parcels. The plaintiff sought administrative relief from, and review of, the valuation of its properties as they appeared on the tentative assesment rolls for the years involved herein by filing with the proper authorities timely protests and applications for correction of the assessments upon the forms supplied by the Tax Commission and in compliance with the laws and requirements of the City and State of New York. The valuations tentatively assessed, the valuations and overvaluations claimed in the protests, and the final valuations found by the Tax Commission, are as follows:

	1938	1939 [1]	1939/1940 [1]	1940/1941 [1]
(a) Valuation tentatively assessed	$411,105,175	$414,635,275	$407,264,800	$403,095,800
(b) Overvaluation claimed in protests	116,628,200	112,642,800	105,683,700	110,722,300
(c) Valuation claimed in protests (a) minus (b)	294,476,975	301,992,475	301,581,100	292,343,200
(d) Final valuation found by Tax Commission	410,985,375	416,628,275	407,040,350	402,707,800

[1] The City of New York interpreted the provisions of the City Charter with respect to this interim period (first half of 1939) as enabling it to reassess the parcels of real estate in their entirety and not merely the additions and retirements. Accordingly the Tax Commission fixed tentative supplemental valuations for 20 parcels of plaintiff's property in the aggregate amount of $284,580,450, of which $236,280,450, was on properties assessed in 1938 and $8,880,000, represented the net valuations of additions less retirements. Plaintiff filed timely and proper applications for correction of the supplemental assessments claiming illegality as well as overvaluations in the aggregate amount of $61,038,000. The Tax Commission found the final assessments in the aggregate amount of $284,580,450.

[1] Although plaintiff's income tax for taxable year 1940 is not involved herein (no refund claims or petitions have been filed for said year) the facts and figures with respect to the real estate taxes assessed and paid during that year are set forth because they affect plaintiff's income tax liability for the year 1941.

16. After they became final, the assessment rolls for these years were duly sent to the Comptroller of the City of New York who, in turn, duly transmitted them, together with his proposed budgets and estimates of receipts, to the City Council. Thereafter the budgets for the years involved were duly adopted and the tax rates for each of those years were duly established by the City Council. The operating budget, as adopted, and the relation thereto of the revenues to be raised through real estate taxes, for each of those years is as follows:

Fiscal year	Council meeting date	From		Total city operating budget	Percent of real estate taxes to total budget
		General funds	Real estate taxes		
1938 [1]	Mar. 1	$134,668,986.18	$465,892,180.46	$599,980,576.64	78.97
1939 [1]	Mar. 3	58,093,696.28	231,694,244.42	289,185,240.80	79.91
1939-40	June 20	115,800,000.00	460,009,526.45	567,809,526.45	79.62
1940-41	June 21	114,300,000.00	466,748,834.10	581,048,834.10	80.33
1941-42	June 24	115,746,227.61	453,994,266.62	573,740,494.13	79.13

[1] Calendar year.
[2] 6 months Jan. 1 to June 30.

17. The plaintiff duly paid the real estate taxes, as billed, for those years and accompanied those payments with letters of protest. All of those tax payments were made under conditions and reservations similar to those for the year 1938, the accompanying letter of which read in part as follows:

> Such payment as to each parcel so assessed is made involuntarily, and under protest and duress, and under compulsion of the penalties provided by law, and to avoid penalties, and to remove the lien of such taxes from the said properties of the undersigned Company. This payment as to each parcel so assessed is made without prejudice, and without admitting the validity of the purported assessments upon the said properties or of the taxes levied thereon, and without waiving any rights which the undersigned Company may have to contest the legality and validity of the said purported assessments, or the overvaluation or inequality in assessments re-

sulting from such purported assessments, or of the taxes levied thereon and imposed upon the said properties and upon the undersigned Company; and the undersigned Company hereby expressly reserves all rights to contest the said purported assessments as to each of such parcels and the said taxes levied thereon upon any and all of the grounds permitted by law.

18. Thereafter the plaintiff duly instituted proceedings for judicial relief and review by filing in the proper court timely petitions to review the final assessments, setting forth, as required by the New York law, the grounds for relief and the respective amounts claimed to be the full and fair value of each individual parcel of property. All of the petitions alleged overvaluation; most of them also alleged inequality and illegality. The allegations of illegality were all based upon illegal method and form except those with respect to the supplemental assessments for the first half of 1939 which were addressed to the entire supplemental assessments.

19. The final assessments of the Tax Commission, the extent to which they were claimed to be overvalued and the full values as alleged in the petitions are as follows:

	1938	1939	1939/1940	1940/1941
(a) Final assessed valuation	$416,985,375	$416,685,375	$407,040,360	$403,707,900
(b) Overvaluation claimed in petitions	[1] 112,536,000	112,042,950	[1] 105,850,700	[1] 110,378,100
(c) Valuations alleged in petitions (a) minus (b)	[1] 304,448,375	304,592,475	[1] 301,189,660	[1] 293,329,800

[1] These amounts are slightly lower than the amounts set forth in the protests (see finding 18) because of the slight reduction in values granted by the Tax Commission.

20. Under the law of New York, the plaintiff was bound by the valuations claimed in its petitions and thereby admitted liability for real estate taxes on the parcels of real estate involved to the extent of the product of the valuations thereon, as alleged, and the established tax rate for the years involved.

21. The protests and the certiorari proceedings with respect to the assessments for the calendar year 1938, the first half of the calendar year 1939, and the fiscal years 1939/1940 and 1940/1941, were bona fide and were filed, instituted, and prosecuted by the plaintiff in good faith.

The valuations therein claimed and asserted by the plaintiff with respect to each of the parcels were bona fide made in dollar amounts which represented the best business judgment of the responsible officers and management of the plaintiff as to the full value of the properties and the amounts that would ultimately be determined by the courts to be correct.

22. In addition to the knowledge and information of its own officers and employees with respect thereto, the plaintiff engaged in the latter part of 1937 outside, independent appraisal experts to make appraisals of all of its properties. While the appraisal job was in progress, the plaintiff's officers and employees had many conferences and were in constant contact with the appraisers, whose reports and working papers were at all times made available to them. The appraisal values, as finally determined by the experts, were generally somewhat lower than the values set forth and claimed by the plaintiff in the protests and in the certiorari proceedings.

23. The certiorari proceedings with respect to the lump sum assessments for the years 1936 and 1937 were settled in the year 1940 for a lump sum amount, thereby avoiding the extended effort and detail necessary to allocate to each individual parcel the amount and basis of that settlement. After those suits were out of the way and in the latter half of 1941, the plaintiff received from the City of New York a proposal which served as a basis for settlement of the then pending certiorari proceedings with respect to the real estate assessments for the years 1938 through 1941.

24. Up to the time that proposal was received, the plaintiff had definitely intended to prosecute the then pending certiorari proceedings to their ultimate conclusion. It was

confidently felt by the officers and management of the plaintiff that the valuations claimed and asserted in the protests and in the certiorari proceedings, supported by certificated opinions of its experts arrived at through application of accepted methods of appraisal, would ultimately be sustained by the courts.

25. The proposal, however, contained a development that was considered very important in that it afforded an opportunity to fix bases and determine methods of assessing the plaintiff's properties in future years in contrast with those employed in prior years that had resulted in expensive litigation. Another important consideration was the matter of public relations—the possible adverse effects of further extended controversy between the plaintiff, a public utility, and the City of New York, a part of the community it served. At that time municipal ownership of gas and electric plants was still a possibility.

26. On the other hand, acceptance of the proposal meant surrender by the plaintiff of part of its claim which it felt justly entitled to and firmly believed would be recovered. It thus became a question of alternatives between continuing litigation and recovering the overpayments of real estate taxes of the past years, or sacrificing a part thereof for the savings and benefits to be derived from an agreeable and harmonious working arrangement and relationship in the future.

27. The plaintiff finally decided that the future benefits warranted acceptance of the proposal and surrender of part of the past values to which it considered itself entitled. The justification of this decision was borne out by the harmonious relationship and valuation stability that existed thereafter until 1947.

28. Accordingly, a stipulation for settlement of the pending proceedings was entered into, which constituted a compromise of the amounts to be recovered by the plaintiff and the valuations to be placed upon each parcel of

real estate owned by the plaintiff. Based thereon the Corporation Counsel of the City of New York executed offers to allow final order, judgment or decree to be entered in said proceedings reducing the assessed valuations as agreed upon; orders thereon were entered with respect to each parcel; and stipulations of discontinuance dated August 29, 1941, were filed with the court. Pursuant thereto the City of New York made refunds to the plaintiff in 1941, aggregating $1,848,679.75, of real estate taxes paid for the years 1938, 1939 and 1940. The settlement also took into account and reduced the assessed valuations for the fiscal year 1941/1942, for which protests had already been filed.

29. The aggregate amounts of the values actually contested, the extent of the reduction, and the extent of the retention of the contested values resulting from the compromise and the stipulations and orders entered thereon, are as follows:

	1938	First half 1939	1939/1940	1940/1941
(a) Claimed overvaluation in the certiorari proceedings	$116,536,000	$112,042,900	$105,859,700	$119,378,100
(b) Amounts by which the contested values were reduced	25,695,000	25,795,000	16,500,000	14,655,000
(c) Amounts of the contested valuations that were retained	90,841,000	86,247,900	89,269,700	104,723,100

30. The amounts and the years in which the real estate taxes were paid and the deductions therefor taken in the plaintiff's income tax returns, are as follows:

Real estate taxes	Paid and deducted in—			
	1938	1939	1940	1941
First half 1938	$6,034,455.26			
Second half 1938	6,032,769.75			
First half 1939		$6,021,790.73		
First half 1939/1940		6,004,087.07		
Second half 1939/1940			$5,973,243.69	
First half 1940/1941			6,022,816.87	
Second half 1940/1941				$5,902,254.04
First half 1941/1942				5,977,127.89
	12,067,225.01	12,025,877.80	11,996,060.56	11,879,381.93

In 1941 the plaintiff paid an additional $5,626,518.25 real estate taxes, which represented the second half of the 1941/1942 real estate taxes, but no deduction for same was taken in its 1941 income tax return.

31. The valuations, as admitted in the plaintiff's protests and petitions for certiorari, as contested therein, and as finally stipulated and adopted by the court, in terms of the real estate taxes set forth in the preceding finding, are as follows:

	1938	1939	1940	Total
(a) Assessed real estate taxes paid and deducted in income tax returns	$12,067,225.01	$12,025,877.20	$11,996,085.56	$36,089,188.37
(b) Admitted liability	8,643,960.47	8,838,859.86	8,649,144.65	26,131,960.98
(c) Contested amount	3,423,238.54	3,187,017.94	3,346,920.91	9,957,177.39
(d) Tax liability determined under court orders	11,308,914.01	11,403,617.55	11,527,957.06	34,240,488.62
(e) Contested amount held valid under court orders (c) minus (f)	2,564,927.54	2,564,757.69	2,578,812.41	8,108,497.64
(f) Contested amount held invalid and refunded in 1941	758,311.00	622,260.25	468,108.50	1,848,679.75

32. The plaintiff was and is under the jurisdiction and supervision of the Public Service Commission of the State of New York (hereinafter referred to as P. S. C.) and kept its books and accounts in accordance with the "Uniform System of Accounts Prescribed for Gas Corporations" and the "Uniform System of Accounts Prescribed for Electric Corporations" established by orders of the P. S. C. dated June 16, 1937 and May 25, 1937, respectively, and in effect during the years involved herein. These Uniform Systems of Accounts constituted full and complete accrual systems of accounting.

33. Paragraph 228 in each of the Uniform Systems of Accounts dealing with Taxes Accrued provides as follows:

> A. This account shall be credited during each accounting period with the amount of taxes accrued during the period, corresponding debits being made to the appropriate accounts for tax charges. Such cred-

its may be based upon estimates, but from time to time during the year as the facts become known, the amount of the periodic credits shall be adjusted so as to include as nearly as can be determined in each year the taxes applicable thereto. Any amount representing a prepayment of taxes applicable to the period subsequent to the date of the balance sheet shall be shown under account 132, Prepayments.

B. The records supporting the entries to this account shall be so kept that the utility can furnish information as to the amount, by classes, of taxes accrued, the basis for each tax accrual and the accounts to which charged, and the amount, by classes, of taxes paid.

34. It was the plaintiff's practice to accrue monthly upon its books its real estate taxes over the period covered by those taxes. These monthly accruals were entered upon the books on the basis of assessments regardless of when or how the payment of those taxes was made. The payment of the taxes had no relation to, or effect upon, such accruals, which were entered both before and after the payment of the taxes. Such accrual of the real estate taxes conforms with the provisions and requirements of paragraph 228 of the Uniform System of Accounts (finding 33) and with the principles of accrual accounting.

35. The accrual method of accounting as recognized by well-established principles of accounting is fundamentally different from the cash basis of accounting. Under a strict cash basis, transactions and events are not recorded until cash has been received or paid, without regard to the period to which they relate or the period in which the revenues or expenses apply. The accrual method, however, is based upon the principle of recording transactions and events as they occur, regardless of when the cash receipts and disbursements part of the activities takes place. Revenues are accrued as nearly as practicable to the period earned, and expenses, which include taxes, are accrued and

allocated in as reasonable and consistent a manner as possible in the period and against the revenues they helped to produce. The primary purpose of accrual accounting principles is to obtain a proper and fair determination of periodic income, often referred to as the process of matching costs against revenues, so that in each accounting period there will be deducted all the ascertainable costs necessary to produce the revenue, including indirect period costs such as depreciation, taxes and interest.

36. Under the accrual method of accounting, the payment of cash extinguishes a liability that either has already been recorded for purposes of determining income or is yet to be recorded for purposes of determining income, but it does not of itself have any effect upon the determination of income. It may either precede or survive the accrual or recordation and is a balance sheet transaction which reduces the cash asset and is balanced by a corresponding reduction of a liability or the substitution of another asset in its place, but it has no effect on the profit or loss—the income determination.

37. When the term "accrual" is used in a balance sheet sense, as distinguished from an income-determining sense, it could never survive payment because payment extinguishes the liability and eliminates it from the balance sheet. But in an income-determining sense, payment has no effect upon accrual which may or may not survive payment depending upon whether the payment is in extinguishment of a liability already accrued or in prepayment of a liability to be incurred, determined, or accounted for at a later date or period.

38. Under accrual accounting, when payment is made with respect to a liability which is denied in whole or in part, the accounting principle as to charges against income would be the same as if payment had not been made; such payment would not affect the treatment of any accruals. This principle applies equally to the payment of

taxes. The payment of the admitted or estimated ultimate liability constitutes the payment of a current charge or expense of operations and the balance of that payment represents an amount estimated to be ultimately recovered and is chargeable to a suspense, deferred debit, or other receivable account. The latter item represents an asset—a deposit which is expected to be recovered.

39. These generally accepted principles of accrual system of accounting apply to the real estate taxes involved herein and are recognized in the Uniform Systems of Accounts prescribed by the P. S. C. (See findings 32 and 33.)

40. In recording the accruals of the real estate taxes on its books, the plaintiff did so solely on the basis of the assessments made and without regard to their payment, or the amounts that were contested, or the amounts which, in the considered judgment of the plaintiff's officers, would ultimately be eliminated. In all instances the accruals upon the plaintiff's books either preceded or survived the payment of the taxes.

41. The accrual on the plaintiff's books on the basis of the assessments without regard to their payment was in accord with the principles of accrual accounting and with the provisions of the Uniform Systems of Accounts promulgated by the P. S. C. However, the accrual on the basis of the assessments without regard to the amounts that were contested, or without taking into consideration the best judgment of management as to the plaintiff's ultimate liability therefor, was not in accord with the principles of accrual accounting or the provisions of the Uniform Systems of Accounts. In its income tax returns for the years 1938, 1939, 1940 and 1941, the plaintiff claimed deductions for the real estate tax items as they were accrued upon its books on the basis of these assessments.

42. The facts as above set forth may be simplified and illustrated by the following example which is applicable to all of the years involved herein:

(a) for the year 1939 plaintiff was notified on January 25, 1939, of a tentative assessment in the amount of	$100.00
(b) within the statutory period and by March 15, 1939, plaintiff, based upon the best judgment of its officers, duly filed a bona fide protest admitting liability of	85.00
and petitioning for an administrative reduction of said tentative assessment of $100 by	15.00
(c) after hearing duly held and on or about May 25, 1939 final assessment was made in the amount of	100.00
(d) thereafter on or about October 1, 1939 under protest and for the stated purpose of avoiding liens, seizures, levies, penalties, interest, etc., and reserving all rights, payment was made of	100.00
(e) within the statutory period, on October 25, 1939, certiorari proceedings were instituted admitting liability in the amount of, and denying liability in excess of	$85.00
(f) on August 21, 1941, the Supreme Court of the State of New York entered its order in said certiorari proceedings fixing the tax liability at	95.00
(g) in October 1941 plaintiff received a refund of the excess payment of	5.00

43. The treatment of this simplified example as accrued on the plaintiff's books, as deducted on the plaintiff's returns, as finally allowed by the Commissioner of Internal Revenue and as contended for by the plaintiff, is illustrated as follows:

1939

Accrued on plaintiff's books	$100.00
Deducted on plaintiff's return	100.00
Deductions allowed by Commissioner	95.00
Deductions contended for by plaintiff	85.00

1941

Added to income by Commissioner	$ 5.00
Deductions contended for by plaintiff	10.00

An alternative contention advanced by the plaintiff is as follows:

(a) if $95 is to be allowed as a deduction in 1939, then the $5 does not constitute income in 1941; and

(b) if the $5 is to be included in the 1941 income, then the deduction for 1939 should be $100.

44. The proper book entries of this example, according to well-recognized and sound principles of accrual accounting, and in accordance with the Uniform Systems of Accounts prescribed by the P. S. C. are illustrated by the following set of entries:

1939

(1) Dr. Tax expense	$85.00	
Cr. Taxes accrued		$ 85.00
(To record the admitted liability for taxes for the year 1939)		
(2) Dr. Taxes accrued	85.00	
Deposit for contested taxes	15.00	
Cr. Cash		100.00
(To record payment of the assessed tax, part of which is contested)		

1941

(3) Dr. Cash	5.00	
Tax expense	10.00	
Cr. Deposit for contested taxes		15.00
(To record final settlement of the contested taxes.)		

45. Under the generally accepted and well-recognized principles of accrual accounting, the $15 in this example, which the plaintiff paid over and above its admitted liability of $85 for taxes in 1939, and which in the best judgment of management would be recovered as soon as full legal proceedings were consummated, would constitute an asset until August 1941 when the settlement was made, and when for the first time the plaintiff had knowledge that instead of an asset of $15 it had only an asset of $5, and that the remaining $10 was, instead, an expense.

46. Under these accrual accounting principles, the $10 expense is accrued and deducted in 1941 and is not related back to 1939 because accrual accounting principles are based, among other things, upon reasonableness and practicability. Under accrual accounting it would be considered unreasonable and impractical to go back and reopen closed years, the income of which had been determined upon an appraisal of all facts then known. Subsequent developments are taken into consideration and recorded in the year

when they occur. If they occur immediately after the end of the year involved and before the books for that year are closed (it usually takes about 30 days to close the books of a substantial business that are kept on an accrual basis), the same practical approach would prompt taking those events into account in the prior year—but aside from this exception, under accrual accounting principles, the facts and developments are recorded in the year they occur.

47. In view of the complex computations involved herein, the parties hereto, without attempting to limit or preclude a determination herein that would involve a computation upon any other basis, have made and agreed upon computations of the amounts of income taxes overpaid or underpaid by the plaintiff, in the event the Court disposes of the issues herein upon any of the following bases:

A. Allowance as deductions in 1938, 1939, 1940 and 1941 of the amounts of real estate taxes admitted in those years to have been due[1] ($85.00); allowance as deductions in 1941 upon termination of the litigation of the additional amounts of taxes determined to be due over and above the amounts previously admitted ($10.00); and exclusion from 1941 income of amounts of excess payments of real estate taxes in said prior years that were refunded in 1941 ($5.00);

B. Allowance as deductions in 1938, 1939, 1940 and 1941 of the amounts of real estate taxes ultimately determined to have been due for said years ($95.00); and exclusion from 1941 income of amounts of excess payments of real estate taxes for said years that were refunded in 1941 ($5.00);

C. Allowance as deductions in 1938, 1939 and 1941 of amounts of real estate taxes paid in those years ($100.00); and inclusion in 1941 income of the amounts of excess payments of real estate taxes for said years that were refunded in 1941 ($5.00).

[1] The figures in parentheses are the comparable figures in the simplified example referred to in finding 42.

Such computations disclose the following underpayments (overpayments) of principal amounts of income taxes made by the plaintiff for the aforesaid years:

	1938—Docket No. 49654	1938—Docket No. 49655	1940 [1]	1941—Docket No. 50433
A	[2] $450,987.74	[2] $434,602.81	$809,412.21	($3,056,708.21)
B			113,346.09	(573,093.73)
C	(138,239.55)	(105,305.58)		

[1] Not before the court herein—computation included to complete the record.
[2] Barred by the statute of limitations except to the extent it may be governed by sec. 3801 of the Internal Revenue Code.

CONCLUSION OF LAW

Upon the foregoing findings of fact, which are made a part of the judgment herein, the court concludes that as a matter of law the plaintiff is entitled to recover, and it is therefore adjudged and ordered that it recover of and from the United States one hundred twenty eight thousand three hundred twenty nine dollars and fifty-five cents ($128,329.55) in case No. 49654; and one hundred five thousand three hundred five dollars and fifty-eight cents ($105,305.58) in case No. 49655, with interest on each amount as provided by law.

The plaintiff is not entitled to recover in case No. 50433 and its petition is therefore dismissed.

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In the Supreme Court of the United States

OCTOBER TERM, 1955

No. 695

CONSOLIDATED EDISON COMPANY OF NEW YORK, INC., PETITIONER

v.

THE UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINION BELOW

The opinion of the Court of Claims (R. 17–25)[1] is reported at 135 F. Supp. 881.

JURISDICTION

The judgment of the Court of Claims was entered on December 6, 1955. The petition for a writ of certiorari was filed on February 16, 1956. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1255 (1).

[1] Record references are to Appendix B of taxpayer's petition.

QUESTION PRESENTED

Where local real estate taxes are assessed and paid in one year and there is a challenge to the amount of the assessment, which is partially successful and results in a refund in a later year, should an accrual basis taxpayer, as the Court of Claims held, compute its federal income taxes by deducting the full amount of the real estate taxes in the year when paid pursuant to the assessment, and include in its income the amount of the refund in the later year when it became entitled to receive it?

STATUTE INVOLVED

Internal Revenue Code of 1939:

> Sec. 23. DEDUCTIONS FROM GROSS INCOME.
>
> In computing net income there shall be allowed as deductions:
>
> * * * * *
>
> (c) *Taxes Generally.*—Taxes paid or accrued within the taxable year, * * *
>
> * * * * *
>
> (26 U. S. C. 1952 ed., Sec. 23.)
>
> Sec. 41. GENERAL RULE.
>
> The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method

employed does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income. * * *

(26 U. S. C. 1952 ed., Sec. 41.)

Sec. 42. PERIOD IN WHICH ITEMS OF GROSS INCOME INCLUDED.

The amount of all items of gross income shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under section 41, any such amounts are to be properly accounted for as of a different period. * * *

(26 U. S. C. 1952 ed., Sec. 42.)

Sec. 43. PERIOD FOR WHICH DEDUCTIONS AND CREDITS TAKEN.

The deductions and credits (other than the corporations dividends paid credit provided in section 27) provided for in this chapter shall be taken for the taxable year in which "paid or accrued" or "paid or incurred", dependent upon the method of accounting upon the basis of which the net income is computed, unless in order to clearly reflect the income the deductions or credits should be taken as of a different period. * * *

(26 U. S. C. 1952 ed., Sec. 43.)

Sec. 48. DEFINITIONS.

When used in this chapter—

* * * * *

(c) *"Paid or Incurred", "Paid or Accrued".*—The terms "paid or incurred" and "paid or accrued" shall be construed according to the method of accounting upon the basis of which the net income is computed under this Part.

* * * * *

(26 U. S. C. 1952 ed., Sec. 48.)

STATEMENT

Taxpayer is a public utility corporation organized and existing under the laws of the State of New York and is engaged in the manufacture, distribution, and sale of electrical energy and gas. (R. 25.) During the years involved (1938, 1939, 1941), it owned several hundred parcels of real estate in the City of New York which were subject to real property taxes under the laws of the State and City of New York.

The procedures established by New York law may be summarized as follows. Parcels are appraised by the City Tax Commission and the determined values are placed upon a tentative assessment roll. Administrative procedures are available to challenge allegedly erroneous valuations. To make a challenge a taxpayer must file an application for correction of assessment (sometimes called a protest) on a form supplied by the Tax Commission, and must reply to all pertinent questions there set forth. One of these questions is, "What do you consider was the full value of the property on January 25 of this

year?" Following exhaustion of the administrative remedy, an unsuccessful applicant may seek judicial review by means of a certiorari procedure. (R. 18.)

A petition for judicial review must set forth the taxpayer's claim as to the correct value of the property involved (except where the taxpayer is challenging the validity of the entire tax). Thus, compliance with New York's provisions relating to administrative protest and to petition for judicial review requires the taxpayer to set forth what he claims to be the full value of the property and to admit liability for real estate tax to that extent. (R. 18.)

The institution or pendency of litigation for the correction of an assessment does not postpone the date on which real estate taxes become due and payable. Moreover, failure to pay the assessed tax when due subjects the property involved to a tax lien and to the possibility of foreclosure. In addition, New York laws imposes a penalty of seven per cent per annum for non-payment. Thus an aggrieved property owner has to pay assessed real estate taxes in the first instance and then seek to rectify any asserted error by pursuing the statutory remedies. Otherwise, the taxpayer runs the risk of having the tax lien foreclosed and the property sold. (R. 18–19.)

Following the procedure outlined above, taxpayer sought administrative relief from, and

review of, the valuations of its properties as they appeared on the tentative assessment rolls for the years involved. After the valuations, as found by the City Tax Commission, became final, taxpayer paid the real estate taxes, as billed for the years 1938–1941, and accompanied the payment with letters of protest. (R. 31–33.) Thereafter, taxpayer duly instituted proceedings in the New York courts for judicial relief and review, setting forth the grounds for relief and the respective amounts claimed to be the full and fair value of each individual parcel of property. All of the petitions alleged, *inter alia,* overvaluation. (R. 33.)

The New York proceedings were compromised by a settlement agreement in 1941, which specified the amounts to be recovered by taxpayer and the valuations to be placed upon each parcel of real estate. Orders were entered thereon and the proceedings discontinued on August 29, 1941. Pursuant thereto, the City of New York made refunds to taxpayer, in 1941, of the excess taxes paid for 1938, 1939, and 1940.[2] (R. 35–36.)

Taxpayer kept its books of account and filed its *federal* income tax returns upon the accrual basis of accounting. (R. 25.) For the calendar years 1938, 1939, and 1941, it filed timely claims for refund which were allowed by the Commissioner

[2] The settlement also took into account and reduced the assessed valuations for the fiscal year 1941–1942, for which protests had already been filed. (R. 36.)

of Internal Revenue in certain amounts that are not here in controversy, but there were offset against these amounts certain sums that are disputed. So far as now pertinent, the Commissioner disallowed portions of the real estate tax deductions, taken in 1938 and 1939, in amounts equivalent to the sums refunded to taxpayer by New York in 1941. The Commissioner included refunded real estate taxes (including a refund of part of the real estate taxes paid in 1940) in taxpayer's gross income for 1941. (R. 26.)

The parties have stipulated that the facts are accurately reflected and illustrated in the following simplified example, for the taxable year 1939, which is applicable to all the years involved. For the year 1939, taxpayer was notified, on January 25, 1939, of a tentative assessment for real estate taxes in the amount of $100. Within the statutory period and by March 15, 1939, taxpayer, based upon the best judgment of its officers, duly filed a bona fide protest admitting liability in the amount of $85, and petitioned for an administrative reduction of the tentative assessment by the amount of $15. After a hearing duly held, and on or about May 25, 1939, final assessment was made in the amount of $100. Thereafter, on or about October 1, 1939, under protest and for the stated purpose of avoiding liens, seizures, levies, penalties, interest, etc., and reserving all rights, taxpayer made payment of the assessed tax in the

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amount of $100. Within the statutory period, on October 25, 1939, certiorari proceedings were instituted in New York admitting liability in the amount of, and denying liability in excess of, $85. On August 21, 1941, the Supreme Court of the State of New York entered its order in the certiorari proceedings fixing the tax liability at $95. In October 1941, taxpayer received a refund of the excess payment in the amount of $5. (R. 41.)

In terms of the example, taxpayer accrued on its books and deducted on its federal tax returns for 1939 the full $100. Upon audit, the Commissioner allowed only $95 for that year, and included the $5 refund received in 1941 as income for 1941.

In the Court of Claims, the taxpayer contended that it should have accrued $85 in the year when the $100 of tax was paid and should have accrued an additional $10 in the year when it became settled that the liability was $95. Alternatively, the taxpayer maintained that if a $95 deduction was proper for 1939, it should not be obliged to include the $5 refund in 1941 income. (R. 19–20.)

The Court of Claims found (R. 38) that it was taxpayer's practice to accrue monthly upon its books its real estate taxes over the period covered by those taxes; that these monthly accruals were entered upon the books on the basis of assessments regardless of when or how payment of those taxes was made; that the pay-

ment of the taxes had no relation to, or effect upon, such accruals, which were entered both before and after the payment of the taxes; and that such accrual of the real estate taxes conformed with the provisions and requirements of the Uniform System of Accounts, prescribed and ordered for gas and electric companies by the Public Service Commission of the State of New York, which constituted full and complete accrual systems of accounting (R. 37, 38).

The court further found, however, that the accrual of the taxes on the basis of the assessments without regard to the amounts that were contested, or without taking into consideration the best judgment of management as to taxpayer's ultimate liability therefor, was not in accord with the principles of accrual accounting or the provisions of the Uniform Systems of Accounts (R. 40, par. 41); that, in terms of the illustration and example given, the proper book entries, "according to well-recognized and sound principles of accrual accounting, and in accordance with the Uniform Systems of Accounts prescribed by the P. S. C.," should show the admitted liability of $85 as an accrual expense in 1939, and the $15 as a deposit for contested taxes which, when settlement was made in 1941, constituted income in the amount of $5 and an accrued expense of $10 (R. 42, par. 44).

Nevertheless, the court concluded that, as a matter of tax accounting, taxpayer was entitled

to deductions in 1938, 1939, and 1941 of the full amounts of real estate taxes paid in those years ($100), and that excess payments of real estate taxes for those years that were refunded in 1941 ($5) should be included in 1941 income. (R. 24, 44.) Translated in dollar amounts in the individual cases, the court concluded that taxpayer was entitled to recover $128,329.55 in Case No. 49654, involving the year 1938; $105,305.58 in Case No. 49655, involving the year 1939; and nothing in Case No. 50432, involving the year 1941, which is the subject of taxpayer's petition herein. (R. 24, 44.)

ARGUMENT

1. The Court of Claims was correct in holding that an accrual basis taxpayer is required to deduct, in the year when paid, local real estate taxes which have been assessed by the appropriate taxing authorities, and that the right to the deduction is not affected by the facts that the taxpayer is contesting, in part, the amount of the assessment and is ultimately successful in securing some refund. The decision is also correct in holding that the taxpayer is required to include in income the amount of the refund which it obtains as a result of the contest, the income to be accrued in the year when the right to it is finally determined.

The principles applied by the Court of Claims are in accord not only with its own prior decision

in *Chestnut Securities Co.* v. *United States,* 62 F. Supp. 574, but also with a consistent line of decisions of the Tax Court, beginning with *Standard-Tilton Milling Co.* v. *Commissioner,* 3 T. C. 1026 (overruling *Elliott Co.* v. *Commissioner,* 45 B. T. A. 82). See also: *Baltimore Transfer Co.* v. *Commissioner,* 8 T. C. 1; *Gibson Products Co.* v. *Commissioner,* 8 T. C. 654; *Western Cartridge Co.* v. *Commissioner,* 11 T. C. 246; *Lehigh Valley Railroad Co.* v. *Commissioner,* 12 T. C. 977; *Taylor Instrument Cos.* v. *Commissioner,* 14 T. C. 388. These principles follow the rule announced by the Internal Revenue Service in G. C. M. 25298, 1947–2 Cum. Bull. 39, 43–44. See also I. T. 3999, 1950–1 Cum. Bull. 129.

Although the taxpayer had actually accrued these real estate taxes on its books and had claimed deductions in its federal income tax returns in the years of payment (R. 23, 41)—the very method which the Court of Claims held to be proper—it now attacks the decision of the court below on the ground that it departs from sound principles of accrual accounting. Indeed, the argument advanced in taxpayer's petition is based largely on the assumption that the tax deductions afforded an accrual basis taxpayer must parallel familiar accounting practices (even though this taxpayer did not follow the particular practice which it now urges). But the short answer is that the accrual basis for tax purposes does not always follow particular ac-

counting practices, even though accepted as a proper or permissible method in the business world. See *Lucas* v. *American Code Co.*, 280 U. S. 445; *Borwn* v. *Helvering*, 291 U. S. 193. In the situation here presented, taxpayer discharged, by payment, the real estate tax liability asserted against it. It could not properly postpone the accrual of some part of this item until a later year, just as though it had continued to have an outstanding liability, when in fact its liability had been discharged by what, as it happens, proved to be an overpayment.

Nor is there any merit in taxpayer's attempt to treat part of its real estate tax payments as though they were merely a deposit of money with the taxing authorities of New York. (Pet. 4–5, 7.) The facts, as found by the Court of Claims, are that the taxpayer "paid" its real estate taxes. (R. 32.) No matter how an accountant might treat the situation—and various accountants might treat it differently—the money was received by the City of New York as a payment of taxes, not as a deposit of money.[3]

[3] The taxpayer is plainly mistaken in the attempt to analogize its situation with that presented by *Security Mills Co.* v. *Commissioner*, 321 U. S. 281, where, in an injunction proceeding, pursuant to court order, the money was deposited by the taxpayer in a bank, designated as a depository of the court, pending final determination of the validity of the tax. In that case, the money was neither paid nor received in satisfaction of the tax liability.

2. The petition cites no decisions which are in conflict with the decision below. *Dixie Pine Co.* v. *Commissioner,* 320 U. S. 516, and *Security Mills Co.* v. *Commissioner,* 321 U. S. 281 (Pet. 6-8, 12-13), holding that there cannot be an accrual of *unpaid,* contested taxes until the liability is finally settled, are not opposed to the decision here. In both cases, the opinions emphasized that the taxes remained unpaid, and, because liability was being contested, it was held that it would be premature to permit the liability to be accrued prior to the time when it became fixed. In the present situation, as we have seen, liability ceased to exist when payment was made, so that the deduction became proper at the time of payment. Neither *United States* v. *Olympic Radio & Television,* 349 U. S. 232, nor *Lewyt Corp.* v. *Commissioner,* 349 U. S. 237, decided anything which is opposed to the decision below.

Finally, *Commissioner* v. *Boylston Market Ass'n,* 131 F. 2d 966 (C. A. 1st), and *Cooperstown Corp.* v. *Commissioner,* 144 F. 2d 693 (C. A. 3d), certiorari denied, 323 U. S. 772, cited in a footnote in the taxpayer's petition (p. 7, fn. 3) and claimed, without amplification, to be in conflict with the decision below (pet. 10), are plainly distinguishable.

The *Boylston* case merely holds that a cash basis taxpayer, which makes a prepayment of expenses for a series of future years, must, as is

true whenever a capital expenditure is made for a wasting asset, amortize the expense over the useful life of the asset.

The *Cooperstown* case involved a cash basis taxpayer who paid a tax and simultaneously sought (and later obtained) its refund. The holding that the payment could not be allowed as a deduction turned on the fact that the tax was paid voluntarily and without any apparent obligation existing. The case has been distinguished on that ground. *Bartlett* v. *Delaney,* 173 F. 2d 535, 540 (C. A. 1st), certiorari denied, 338 U. S. 817; *Baltimore Transfer Co.* v. *Commissioner,* 8 T. C. 1, 7. Indeed, the Tax Court, which follows the rule applied by the Court of Claims in this kind of case, has also followed the *Cooperstown* case where similar circumstances were presented. *Kenyon Instrument Co.* v. *Commissioner,* 16 T. C. 732, 741–742; *Hart Furniture Co.* v. *Commissioner,* 12 T. C. 1103, 1107–1108, reversed on other grounds, 188 F. 2d 968 (C. A. 5th).

3. The brief of the *amicus curiae,* being filed on behalf of the New York Telephone Company in support of the petition, cites two additional authorities which are claimed to be in conflict with the decision of the Court of Claims in this case, *Inland Products Co.* v. *Blair,* 31 F. 2d 867 (C. A. 4th), and *Bergan* v. *Commissioner,* 80 F. 2d 89 (C. A. 2d).

While, in a technical sense, these early cases are opposed to the views of the court below, we doubt that they represent the kind of contemporary conflict in decisions which requires review by this Court at this time. Both cases were decided before this Court's decisions in *Dixie Pine Co.* v. *Commissioner,* 320 U. S. 516, and *Security Mills Co.* v. *Commissioner,* 321 U. S. 281. Neither the Second Circuit nor the Fourth Circuit has had an opportunity to reexamine the soundness of those decisions in the light of more recent developments. It may be that, when the question is squarely presented, those courts, like the Tax Court in *Stanard-Tilton Milling Co.* v. *Commissioner,* 3 T. C. 1026 (overruling *Elliott Co.* v. *Commissioner,* 45 B. T. A. 82), will conclude that these earlier decisions should no longer be followed and that they should apply the principles which are now being consistently followed by the Tax Court, the Court of Claims, and the Commissioner. Indeed, we are informed that the New York Telephone Company intends to test this issue in a refund suit in the District Court for the Southern District of New York. Accordingly, the Second Circuit may soon have the opportunity of stating its present position.

Under the circumstances, we believe that the conflict in decisions which the *amicus curiae* brings to the Court's attention is not ripe for consideration by this Court. We also observe that the *amicus curiae* is urging a position which

is different from that argued by the taxpayer. We believe that it would be preferable for the Second Circuit to express its views on the merits of that position before this Court is asked to consider it.

CONCLUSION

The decision below is correct. There are no conflicting decisions which require review by this Court at the present time. Accordingly, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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HAROLD B. WILLEY, Cl

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1955

No. 695

CONSOLIDATED EDISON COMPANY OF NEW YORK, INC.,
Petitioner,

v.

THE UNITED STATES OF AMERICA,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

REPLY BRIEF OF PETITIONER

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REPLY BRIEF OF PETITIONER

The Government's restatement of the facts is correct except for the statement (p. 9) that the Court below found that under well-recognized and sound principles of accrual accounting and the Uniform Systems of Accounts prescribed by the Public Service Commission of the State of New York the $5 in the illustrative example constituted income in 1941. On the contrary the Court found that under those principles the $5 did *not* constitute income in 1941 (Pet., Appendix B, p. 42, Par. 44, 45).

The petition filed herein is predicated primarily upon the fact that the Court below disregarded the principles of accrual and the construction of the accrual provisions of the Internal Revenue Code as established by this Court, and has rendered a decision contrary thereto. The Government's brief in opposition does not address itself to the

gravamen of the petition and fails to disprove the validity of the reasons advanced by the petitioner for the granting of the writ. To avoid confusion, the order in which these reasons are set out in the petition will be adhered to.

1. The decision of the Court below is contrary to the principles of accrual and statutory construction established by this Court.

The Government's only answer to that part of this reason which is based on *United States* v. *Olympic Radio & Television, Inc.*, 349 U. S. 232, and *Lewyt Corporation* v. *Commissioner*, 349 U. S. 237, 242-243, is the bare statement that neither case "decided anything which is opposed to the decision below" (p. 13). Ignored completely is the presentation of the principles of accrual and the statutory construction of the accrual sections of the Internal Revenue Code which were the bases for the decisions in those cases. (See pet. 8).

The sole basis of the Government's argument in answer to that part of this reason which is based on *Dixie Pine Products Co.* v. *Commissioner*, 320 U. S. 516, and *Security Flour Mills Co.* v. *Commissioner*, 321 U. S. 281, is the fact that petitioner *paid* the taxes while denying and contesting its liability for them.

One prong of this argument is the Government's statement that "In both cases, the opinions emphasized that the taxes remained unpaid * * *" (p. 13)—the implication being that had the taxes been paid the opinions indicate an opposite conclusion would have been reached. Neither the statement nor the implication is borne out by the opinions.

The only reference to unpaid taxes in *Dixie Pine* is when this Court adverted to the "all events" test.[1] The crux

[1] 320 U. S. 516, 519 "It has long been held that in order to truly reflect the income of a given year, all the events must occur in that year which fix the amount and the fact of the taxpayer's liability for items of indebtedness deducted though not paid".

of the decision in *Dixie Pine* is that a taxpayer, contesting liability

> "must, in the circumstances, await the event of the state court litigation and might claim a deduction only for the taxable year in which its liability for the tax was finally adjudicated". 320 U. S. 516, 519.

There is no suggestion whatever, as the Government implies, that had payment been made while the contest was in progress the taxpayer would have become entitled to a deduction prior to the year its liability for the tax was finally adjudicated.

In *Security Flour Mills* the issue before this Court was whether the taxpayer could relate back to 1935 rebates made to its customers in 1936, 1937 and 1938 of part of the purchase price they had paid in 1935, which represented the amount of Agricultural Adjustment Act taxes the taxpayer had figured in its cost of goods sold. The question whether the taxpayer had or had not paid the AAA taxes had nothing to do with this issue. To argue, as the Government does, that this Court "emphasized that the taxes remained unpaid" (p. 13) is to misread the opinion in that case.

The other prong of the Government's argument is the statement (p. 13) "In the present situation, as we have seen, liability ceased to exist when payment was made, so that the deduction became proper at the time of payment".[2] Inherent in the Government's stress of payment as the basis for accrual is an acknowledgment that at least up to the time of payment, the contested liability, under *Dixie Pine*, was contingent and accrual had to await the

[2] The Government's brief had previously stated (p. 12) that "• • • taxpayer discharged, by payment, the real estate tax liability asserted against it"; taxpayer could not postpone accrual "when in fact its liability had been discharged by • • • an overpayment"; and "The facts, as found by the Court of Claims, are that the taxpayer 'paid' its real estate taxes".

outcome of the litigation. But the payment did not terminate the litigation—the ultimate extent of the liability was yet to be determined in the pending litigation.[3] To say, as the Government does, that petitioner's "liability ceased to exist when payment was made" is to fail the grasp the holding of *Dixie Pine* for, to the extent that the liability is contested, it never does exist for purposes of accrual—it is contingent upon the outcome of the pending litigation. It therefore could not have "ceased to exist" when the payment was made.

2. The importance of the question.

Apparently the Government agrees with the petitioner as to the importance of the question for it submits nothing in opposition.

3. The decision of the court below is erroneous on its own facts and reasoning.

In answer to this reason the Government states (pp. 10-11) that "The principles applied by the Court of Claims are in accord not only with its own prior decision in *Chestnut Securities Co.* v. *United States*, 62 F. Supp. 574, but also with a consistent line of decisions of the Tax Court, • • • [citing cases]".

But the Government makes no attempt to explain the change in the basis of the decision of the Court below from that of *Chestnut Securities* (see pet. 11-12).

The Government's claim that the decision is in accord with a consistent line of Tax Court cases does not bear up upon scrutiny of those cases or consideration of the decision in the light of the briefs submitted to the Court below.

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[3] Petitioner's payment in the instant case only removed the possibility of foreclosure and seizure of its property by the City of New York. The involuntary nature of the payment is also overlooked by the Government.

There, the Government cited the very same cases it now cites, in support of its contention that *Chestnut Securities* had been followed by the Tax Court on the principle that payment of an unadmitted and contested tax liability accrues that liability. In reply thereto petitioner showed that *not a single one of these cases followed Chestnut Securities* on this question. The absence from the opinion of the Court below of any reference to, or reliance upon, these cases is not without significance.

In relying upon GCM 25298, 1947-2 C. B. 39, 43-44, (p. 11) the Government is attempting to raise itself by its own bootstraps because that ruling was issued to the petitioner in the denial of the very claim now before this Court. The Commissioner has not been entirely consistent with respect to the principle on which this GCM is based. He has adopted an inconsistent position and has modified this GCM in Mim. 6444, 1949-2 C. B. 11,[4] a fact entirely overlooked in the Government's brief. Moreover, since the Court of Claims has in effect disavowed in its decision the basis of the *Chestnut Securities* decision upon which the GCM was predicated (pet. 11-12), the very foundation of the GCM is now removed. The Commissioner may not by merely issuing a ruling perpetuate an error especially when it is contrary to principles of accrual and statutory construction established by this Court. *Bingham's Trust* v. *Commissioner,* 325 U. S. 365, 376-377, (1945); *Manhattan General Equipment Co.* v. *Commissioner,* 297 U. S. 129, 134-135, (1936).

In view of all of the foregoing, it is submitted that the Government has failed to refute the reasons advanced by

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[4] 1949-2 C. B. 11—"Where payment of a tax is required as a prerequisite to further appeal, such payment is not to be regarded as a payment of a demanded tax deficiency". There is no logical distinction between payment of an unadmitted and contested tax liability to enable the taxpayer to prosecute an appeal and payment of an unadmitted and contested tax liability to prevent a tax lien upon, and the foreclosure and seizure of, the taxpayer's property.

petitioner for the granting of the writ and has failed to show why a writ of certiorari to the United States Court of Claims should not be granted.

Respectfully submitted,

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THE UNITED STATES,

Respondent.

BRIEF OF *AMICUS CURIAE* IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS.

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BRIEF OF *AMICUS CURIAE* IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS.

This Brief is filed, with the consent of both Petitioner and Respondent, on behalf of New York Telephone Company, 140 West Street, New York, New York.

Reasons for filing this Brief.

The Federal income and profits taxes of New York Telephone Company for the years 1940-1945 raise the same questions that are presented in the Consolidated Edison case. The case of the Telephone Company involves a very large amount of tax, and the effect on it of the decision of the Court of Claims in the Consolidated Edison case would be, in our opinion, extremely harsh and unreasonable.

The factual situation in the Telephone Company case, except for amounts involved, is substantially the same as that presented in the Consolidated Edison case. That is, for the years 1936-1939 the City of New York made excessive real estate tax assessments on the properties of the Telephone Company. The Telephone Company was obliged to pay these assessments because otherwise liens would have attached which could have been foreclosed and the properties sold, and the Company would have been subject to penalty interest of 7% per annum. (Finding 13, Pet., p. 30.)[1] There was no way of avoiding these oppressive consequences except to pay the assessments, even though there was every reason to believe they were excessive and that a substantial part of the amount paid later would be refunded.[2]

The Telephone Company promptly instituted judicial proceedings contesting the assessments. These proceedings were terminated in 1944 under an order of the Supreme Court of the State of New York reducing the assessments for each of the years 1936-1939. This order was entered pursuant to a stipulation embodying an offer made by the City and accepted by the Company. Under the settlement the City refunded over $3,500,000 of the amounts paid as real estate taxes for those years.

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[1] Payments under these conditions, as a matter of law, are considered as made, not voluntarily, but under duress and coercion. *Adrico Realty Corporation* v. *City of New York*, 250 N. Y. 29, 164 N. E. 732 (1928); *Goldberg* v. *New York*, 260 App. Div. 61, 20 N. Y. Supp. 2d 801 (1940), aff'd without opinion, 285 N. Y. 705 (1941).

[2] One of the main reasons for the excessive assessments was a claim by the City that the many separate parcels of the Telephone Company could be assessed in bulk, and that so assessed they had a value much greater than the total of the separate assessments. The courts of New York gave short shrift to this contention. *People ex rel. Brooklyn Union Gas Co.* v. *Miller*, 172 Misc. 169, 14 N. Y. Supp. 2d 444 (1939), aff'd without opinion, 258 App. Div. 1066, 17 N. Y. Supp. 2d 1022 (1940).

The Federal excess profits taxes of the Telephone Company for the years 1940-1945 were determined on the average earnings basis. That is, the excess profits tax credit of the Telephone Company was calculated on the basis of its average earnings for the base period years 1936-1939,—the years in which the excessive real estate tax assessments were paid.

If the Telephone Company is required to take Federal income tax deductions in the years 1936-1939 for the amounts paid as real estate taxes in those years which were erroneously and illegally assessed and collected, and which were later refunded by the City, the Federal excess profits tax credit of the Company will be reduced and its excess profits taxes for all of the years 1940-1945 will be very substantially increased.

It is for this reason that the decision of the Court of Claims in the Consolidated Edison case produces in the case of the Telephone Company a situation which is extraordinarily serious and which it is difficult to believe the law intended. *The result would be to impose on the Telephone Company a severe Federal tax penalty because of the error of the City taxing authorities in asserting taxes which they later conceded to be improper.* While we are not pressing this as a reason for granting the writ, we nevertheless believe it might be helpful to the Court, in considering the Petition, to be aware that such erratic consequences flow from the Court of Claims decision.

Issues raised in the Consolidated Edison case.

For simplicity of illustration and discussion the parties there assumed the hypothetical case of a real estate tax assessment in 1939 of $100; payment of this amount in that year; admission by the taxpayer of a liability of $85 and

a contest by it as to $15; final judicial determination in 1941 of a liability of $95, and a refund in 1941 of $5 (Pet., p. 19). Three possible ways of handling this situation, for Federal income and profits tax purposes, were submitted to the Court of Claims (Finding 47, Pet., p. 43), viz.:

Basis A. Allow deductions of $85 in the earlier year of payment and of $10 in the later year of termination of contest, and exclude from income the $5 refunded in the later year.

Basis B. Allow deduction of $95 (the amount ultimately determined to have been due) in the earlier year of payment, and exclude from income the $5 refunded in the later year of termination of contest.

Basis C. Allow deduction of the entire $100 in the earlier year of payment, and include in income for the year of termination of contest the $5 refunded in that year.

The Court of Claims held in favor of Basis C and rejected Bases A and B (Pet., p. 24). In its Petition for a Writ of Certiorari Consolidated Edison argues that this decision is contrary to decisions of this Court and that, under those decisions and for other reasons, Basis A is the proper basis.

Without in any way questioning the position of Consolidated Edison, New York Telephone Company desires to point out that the decision of the Court of Claims in upholding Basis C is to the effect that Basis B is not the proper basis. And we respectfully submit to the Court that this decision of the Court of Claims, rejecting Basis B, is in conflict with decisions in the Second, Third and Fourth Circuits. For this reason we urge the Supreme Court should grant certiorari.

Certiorari should be granted because, in rejecting Basis B, the decision of the Court of Claims is in conflict with decisions of the Second, Third and Fourth Circuits.

The conflicting decisions referred to are *Inland Products Co.* v. *Blair,* 31 F. 2d 867 (4th Cir. 1929); *Bergan* v. *Commissioner,* 80 F. 2d 89 (2d Cir. 1935); and *Cooperstown Corporation* v. *Commissioner,* 144 F. 2d 693 (3d Cir. 1944), cert. den., 323 U. S. 772 (1944).

These decisions hold that, if a taxpayer makes a payment in respect of a tax and, for Federal income tax purposes, takes a deduction for such payment, and later it is determined that the taxpayer was not obligated to make the payment and it is refunded, if the statute of limitations on the assessment of additional income tax for the year of deduction has not yet run, the deduction must be reduced by the amount of the refund, and the refund is not income for the year in which received. That is, these decisions in the Second, Third and Fourth Circuits hold that the proper way to handle the matter is as set forth in Basis B of Finding 47 (Pet., p. 43).

The decisions go on the theory that the question is one of correcting a mistake, and since the amount refunded was not due, it was not a payment of a "tax" and, therefore, it was not deductible when paid. See *Inland Products Co., supra,* at p. 868; *E. B. Elliott Co.,* 45 B. T. A. 82 (1941). The decisions are in accord with administrative practice which appears to have been consistently followed by the Commissioner for over thirty years.[3]

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[3] O. D. 741, 3 C. B. 115 (1920); S. M. 4683, V-1 C. B. 59; I. T. 2578, X-1 C. B. 119; Mim. 3958, XI-2 C. B. 33; I. T. 2741, XII-2 C. B. 48. Cf. Mim. 6444, 1949-2 C. B. 13; G. C. M. 26211, 1949-2 C. B. 112. It will be noted the later rulings, reversing the Commissioner's prior position, were issued years after the taxable years involved in the Consolidated Edison and Telephone Company cases.

It is necessary to consider the significance, for present purposes, of this Court's decision in *Security Flour Mills Co.* v. *Commissioner,* 321 U. S. 281 (1944). That case was decided after *Inland Products Co.* v. *Blair, supra,* and *Bergan* v. *Commissioner, supra,* and before *Cooperstown Corporation* v. *Commissioner, supra.*

Security Flour Mills denied to a taxpayer the right to relate back against cost of goods sold such part of a refund of processing taxes made in a later year, after the Agricultural Adjustment Act had been declared unconstitutional, as the taxpayer voluntarily, for reasons of maintaining goodwill, turned over to a few favored customers which had paid to it an amount equivalent to the tax, not as a tax but as part of the purchase price of the goods. It presented an attempt to give retroactive effect to subsequent voluntary acts of the taxpayer, and it did not involve an adjustment in the light of later knowledge that in fact there was no liability for a payment made as a tax in an earlier year.

Since *Security Flour Mills* involved a situation significantly different from that presented in *Inland Products Co.* v. *Blair* and *Bergan* v. *Commissioner,* we submit *Security Flour Mills* does not overrule those decisions.

As noted, *Security Flour Mills* preceded *Cooperstown Corporation* v. *Commissioner.* In *Cooperstown* the corporate taxpayer, owning substantial assets and having substantial income, filed a Federal capital stock tax return for 1937, paid the tax shown on it to be due, and took the capital stock tax as a deduction. Subsequently, it filed a claim for refund of the capital stock tax, on the ground that it was not subject to the tax because it was not "doing business"—often a very close question. The claim was allowed and the capital stock tax was refunded in 1939. The taxpayer took the refund into income for 1939, but the Commissioner insisted it must be related back to eliminate

the deduction claimed in the earlier year.[4] The Commissioner took the position that, even though the taxpayer thought it was liable for the tax, since it was mistaken it could not take a deduction for the payment. The Third Circuit upheld the Commissioner, and in the course of its opinion referred to the line of cases with which the instant case is in conflict. Thereafter, the Supreme Court decided *Security Flour Mills*. In view of this decision, the Third Circuit, on its own motion, granted a rehearing, after which it decided that its original conclusion was right. The taxpayer appealed to this Court for review and *certiorari* was denied, 323 U. S. 772 (1944).

It may be suggested that *Cooperstown* is not in point here because there the taxpayer *voluntarily* made a payment as a tax which it thought was due but which actually was not due, and it may be contended that only under such extraordinary circumstances should the mistake be corrected in the year in which it was made. But, in fact, the circumstances in the *Cooperstown* case were not extraordinary. In this country, where many taxes are self-assessed, in the nature of things many, probably most, cases of tax refunds result from *voluntary* overpayments by taxpayers. In *Inland Products Co.* v. *Blair, supra,* the Circuit Court found the amounts were "paid voluntarily by the taxpayer under mistake of law." (p. 868) This conclusion defies making any distinction between *Inland Products Co.* and *Cooperstown*. Except for a refund resulting from retroactive legislation, *any tax refund is an admission of a mistake*. Who made the initial mistake, whether the taxpayer or the taxing authorities, and how quickly the mistake is corrected, would seem wholly irrelevant.

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[4] Apparently, this position in that case had the effect of benefiting the revenue, since it resulted in not only an additional income tax for the earlier year but also a heavy personal holding company surtax for that year.

It is therefore submitted that *Cooperstown* is squarely in conflict with the instant case. And since *Cooperstown* was decided after *Security Flour Mills,* and since the Supreme Court denied certiorari in *Cooperstown,* it cannot be said that *Security Flour Mills* resolved the very clear cut conflict which now exists.

What, we submit, is an erroneous view as to the scope of the *Security Flour Mills* decision was expressed by the First Circuit in *Bartlett* v. *Delaney,* 173 F. 2d 535 (1st Cir. 1949), cert den., 338 U. S. 817 (1949). However, the facts of the *Bartlett* case did not raise the issue as to the treatment of a payment made as a tax. Since this Court denied certiorari in *Bartlett,* as it did in *Cooperstown,* presumably it considered that the decision in *Bartlett* was not in conflict with the decision in *Cooperstown.*

It is now impossible to tell whether the decision of the Court of Claims in the instant case and the views expressed by the First Circuit in its opinion in the *Bartlett* case, on the one hand, or the above cited decisions of the Second, Third and Fourth Circuits, on the other hand, represent the correct view with respect to what is an important and constantly recurring question in the administration of the internal revenue laws. It is submitted that, in order to resolve this conflict, the Court should grant certiorari in this case.

Conclusion.

The Petition for a Writ of Certiorari should be granted, and this Court should review all three theories presented to the Court of Claims.

Respectfully submitted,

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